

REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON MIER LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Mier Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2014, the statements of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Property Plant and Equipment

6. I was unable to obtain sufficient appropriate audit evidence for the carrying values of landfill sites included in the annual financial statements, as the methods and assumptions applied to determine the value of the landfill sites could not be confirmed. I was unable to confirm the carrying values of municipal landfill sites by alternative means. Consequently I was unable to determine whether any adjustment relating to land disclosed in note 7 stated at R95 268 626 (2013: R95 268 626), furthermore I was unable to determine whether any adjustment relating to the provision and expenditure

relating to landfill sites in the annual financial statements was necessary.

7. The municipality did not accurately disclose the property plant and equipment in note 7 to the financial statements. This resulted in property plant and equipment being overstated by R1 469 305. Additionally, there is a consequential impact on the surplus and accumulated surplus for the period.

Revenue from exchange and non-exchange transactions

8. I was unable to obtain sufficient appropriate audit evidence for the service charges included in the annual financial statements, as audit evidence could not be submitted to determine the reasonableness of estimated water consumption charged during the year. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustment relating to the services charges, water revenue, stated at R2 498 563 (2013:R2 910 391) in the annual financial statements was necessary.
9. The municipality did not have adequate systems in place to ensure that all municipal consumers are charged for water, sanitation and refuse during the year, as required by GRAP 9, *Revenue from Exchange Transactions*. I was unable to quantify the amount of misstatement on the annual financial statements as it was impracticable to do so, consequently revenue from exchange transactions and trade and other receivables from exchange transactions is misstated with an undetermined amount. Additionally, there is a consequential impact on the surplus and accumulated surplus for the period.
10. The municipality did not recognise profit shares to be received from agreements entered into with third parties, as required by GRAP 9, *Revenue from Exchange Transactions*. I was unable to quantify the amount of misstatement on the annual financial statements as it was impracticable to do so, consequently revenue from exchange transactions and trade and other receivables from exchange transactions are understated with an undetermined amount. Additionally, there is a consequential impact on the surplus and accumulated surplus for the period.
11. The municipality did not charge interest on arrear consumer accounts, as required by the MFMA section 64, Revenue Management and the fair value principals of revenue as set out in GRAP 9 and 23 for *Revenue from Exchange and Non – Exchange Transactions*. I was unable to quantify the amount of the misstatement on the annual financial statements as it was impracticable to do so, consequently revenue from exchange transactions and trade and other receivables from exchange and non - exchange transactions are understated with an undetermined amount. Additionally, there is a consequential impact on the surplus and accumulated surplus for the period.

Payables from Exchange Transactions

12. I was unable to obtain sufficient appropriate audit evidence for the salary control account included in the annual financial statements, as audit evidence could not be submitted for the control account. I was unable to confirm the trade and other payables from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments relating to the payables from exchange transactions, stated at R1 615 834 (2013: R3 462 445) in the annual financial statements was necessary.

Receivables from Exchange and Non - Exchange Transactions

13. I was unable to obtain sufficient appropriate audit evidence for the provision for impairment included in the annual financial statements, as the provision have not been

calculated as the difference between the asset's carrying amount and the present value of estimated future cash flows as required by GRAP 104, *Financial Instruments*. I was unable to confirm the provision for impairment by alternative means. Consequently, I was unable to determine whether any adjustments relating to the receivables from exchange and non - exchange transactions, stated at R5 322 990 (2013: R6 101 733) and the movement in the impairment provision, stated at R1 691 418(2013: R2 541 300) in the annual financial statements was necessary.

Consumer deposits

14. The municipality did not charge consumer deposits as required by the Credit Control Policy adopted by council for the municipality for the current and prior year. Consequently, I was unable to quantify the amount of the misstatement on the annual financial statements as it was impracticable to do so. Additionally, there is a consequential impact on the accumulated surplus for the period.

Inventory

15. The municipality did not have adequate systems in place to monitor and report on water losses for the current and prior year, as required by the section 125 of the MFMA. Consequently, no disclosure was made in the annual financial statements; I was unable to quantify the amount of the misstatement on the annual financial statements as it was impracticable to do so. Additionally, there is a consequential impact on water inventory, the surplus and accumulated surplus for the period.
16. I was unable to obtain sufficient appropriate audit evidence regarding inventory as the municipality does not have adequate systems in place. I was unable to confirm the inventory by alternative means. Consequently I was unable to determine whether any adjustment relating to inventory stated at R712 186 in the financial statements was necessary.

Budget disclosure

17. The approved adjustment budget as stipulated in GRAP 24, Presentation of budget information in the AFS was not properly disclosed in the financial statements, as the structure of the budget comparison is not aligned to the financial statements.

Cash Flow Statement

18. I was unable to obtain sufficient appropriate audit evidence that management had properly disclosed the cash flow statement relating to the current and prior year. I was unable to confirm the cash flow statement by alternative means. Consequently, I was unable to determine whether any adjustment to the cash flow statement amounts were necessary.

Qualified opinion

19. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Mier Local Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

20. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Significant uncertainties

21. With reference to note 47 to the financial statements, the municipality is the defendant in several lawsuits. The ultimate outcome of the matters cannot presently be determined and no provision for any liability that may result has been made in the financial

statements.

Restatement of corresponding figures

22. As disclosed in note 36 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of errors discovered during 2014 in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Going concern

23. The Note 52 to the financial statements indicates that the municipal budget was overspent by R9 387 899 during the year ended 30 June 2014 and, as of that date, the municipality's current liabilities exceeded its current assets by R7 287 282. These conditions, along with other matters as set forth in the note 52, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

Additional matters

24. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

25. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Supplementary explanations of budget variances presented outside the financial statements

26. The supplementary explanations of budget variances contained in the statement of comparison of budgeted and actual amounts do not form part of the financial statements. I have not audited these explanations and accordingly I do not express an opinion thereon

Unaudited supplementary schedules

27. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

28. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for the selected development priorities presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

29. The annual performance report was not presented for auditing and consequently my findings below are limited to the procedures performed on the strategic planning and performance management documents for the following selected development priorities:

- Development Priority 1: Water and Sanitation – page x

- Development Priority 2: Roads and Transport – page x
- Development Priority 3: Housing – page x

30. I assessed the information to determine whether the performance indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).

31. The material findings in respect of the selected development priorities are as follows

Development Priority 1: Water and Sanitation

Usefulness of performance information

32. Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific.

- Performance targets must be measurable. I could not measure the required performance for 100% of the targets.
- The period or deadline for delivery of targets must be specified. A total of 100% of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
- Performance indicators must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions. Management also did not implement a sufficient process for reporting on predetermined objectives.

33. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. Performance indicators did not to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the 100% indicators could not be assessed due to a lack of corroborative supporting evidence to verify management's explanation why the indicators were considered important and relevant to the realisation of strategic goals and objectives.

Development Priority 2: Roads and Transport

Usefulness of performance information

34. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific.

- Performance targets must be measurable. I could not measure the required performance for 100% of the targets.
- The period or deadline for delivery of targets must be specified. A total of 100% of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
- Performance indicators must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions. Management also did not implement a sufficient process for reporting on predetermined objectives.

35. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. Performance indicators did not to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the 100% (>20%) indicators could not be assessed due to a lack of corroborative supporting evidence to verify management's explanation why the indicators were considered important and relevant to the realisation of strategic goals and objectives.

Development priority 3: Housing

Usefulness of performance information

36. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific.
- Performance targets must be measurable. I could not measure the required performance for 100% of the targets.
- The period or deadline for delivery of targets must be specified. A total of 100% of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
- Performance indicators must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions.

37. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. Performance indicators did not to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the 100% indicators could not be assessed due to a lack of corroborative supporting evidence to

verify management's explanation why the indicators were considered important and relevant to the realisation of strategic goals and objectives.

Compliance with legislation

38. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA are as follows:

Strategic planning and performance management

- 39. The municipality did not establish a performance management system, as required by section 38(a) of the Municipal Systems Act (MSA).
- 40. The municipality did not conduct its affairs in a manner which was consistent with its integrated development plan, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6.
- 41. The accounting officer of the municipality did not by 25 January assess the performance of the municipality during the first half of the financial year, as required by section 72(1)(a)(ii) of the MFMA.
- 42. A performance audit committee was not in place and the audit committee was not used to fulfil the performance audit committee function, as required by Municipal planning and performance management regulation 14(2)(a).
- 43. The annual performance report for the financial year under review was not prepared, as required by section 46 of the MSA and section 121(3)(c) of the MFMA.
- 44. The municipality did not have and maintain effective, efficient and transparent systems of financial and risk management and internal controls as required by section 62(1)(c)(i) of the MFMA.

Budgets

- 45. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 / 87(8) of the MFMA.
- 46. Quarterly reports were not submitted to the council on the implementation of the budget and financial state of affairs of the municipality within 30 days after the end of each quarter, as required by section 52(d) of the MFMA.

Annual Report and Annual Financial Statements

- 47. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of sections 122 of MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a qualified audit opinion.
- 48. The annual report for the year under review does not include; assessment of the municipality's performance against measurable performance objectives for revenue collection from each revenue source and for each budget vote and the report from the audit committee, as required by section 121(3)(f) and (j) and 121(4)(g) of the MFMA.
- 49. The annual report for the year under review does not include the report of the audit committee, as required by MFMA 121 (3) (j) and 121 (4) (g).

Audit Committee

50. An audit committee was not in place, as required by section 166(1) of the MFMA.

Internal Audit

51. The internal audit unit did not function as required by section 165(2) of the MFMA, in that:

- it did not prepare a risk-based audit plan and an internal audit programme for the financial year under review.
- it did not report to the audit committee on the implementation of the internal audit plan.
- it did not advise the accounting officer and report to the audit committee on matters relating to internal audit, internal controls, accounting procedures and practices, risk and risk management and loss control.

52. The internal audit unit did not advise the accounting officer and report to the audit committee on matters relating to compliance with the MFMA, the DoRA and other applicable legislation, as required by section 165(2)(b)(vii) of the MFMA.

Expenditure Management

53. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.

54. Payments were made without the approval of the accounting officer or a properly authorised official as required by section 11(1) of the MFMA.

55. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the Municipal Finance Management Act.

Revenue Management

56. A credit control and debt collection policy was not maintained and implemented, as required by section 96(b) of the Municipal Systems Act and section 62(1)(f)(iii) of MFMA.

57. An adequate management, accounting and information system which accounts for revenue was not in place, as required by section 64(2)(e) of the MFMA.

58. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

59. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.

60. Accounts for municipal tax and charges for municipal services were not prepared on a monthly, as required by section 64(2)(c) of the MFMA.

61. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Liability Management

62. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.

Consequences Management

63. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.
64. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.
65. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

Human resource management

66. The Acting Municipal Manager, Chief Financial Officer and other senior managers directly accountable to the municipal manager were appointed for a period of more than six months, in contravention of section 54A(2A) the MSA.
67. The municipal manager and senior managers directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) MSA.
68. The municipality did not develop and adopt appropriate systems (policies) and procedures to monitor measure and evaluate performance of staff in contravention of MSA section 67(d).

Procurement and contract management

69. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
70. Bids were not always evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality as required by SCM regulation 28(2).
71. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act and CIDB regulation 18.
72. The prospective providers list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualify for listing, and prospective providers were not invited to apply for such listing at least once a year as per the requirements of SCM regulation 14(1)(a)(ii) and 14(2).
73. Quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
74. Quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

Conditional grants received

75. The municipality did not evaluate its performance in respect of programmes funded by the Municipal Infrastructure Grant, Local Government Financial Management Grant and Municipal Systems Improvement Grant or submit the evaluation to the transferring national officer within two months after the end of the financial year, as required by section 12(5) of the DoRA.

Internal control

76. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant deficiencies that resulted in the basis for a qualified opinion, the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

Leadership

77. Senior management of the entity did not set the correct tone at the top. Senior management did not adhere to internal controls, which resulted in various instances of irregular, fruitless and wasteful and unauthorised expenditure being incurred and other material misstatements in the financial statements, not detected by management.
78. The accounting officer did not ensure that internal control procedures were developed, implemented and monitored to ensure that monthly sets of GRAP financial statements were prepared and subjected to review.
79. The accounting officer did not communicate the commitment to quality in preparing the annual financial statements.
80. Actions plans to address prior year audit findings were not prepared by the leadership of the municipality resulting in the reoccurrence of material misstatements in the annual financial statements and unresolved matters from prior year audits, affecting the auditor's opinion.

Financial and performance management

81. Management did not review the financial statements, to ensure the achievement of fair presentation; this resulted in material amendments to the financial statements.
82. Specific training interventions are needed in the municipality to enable finance staff members to understand and implement the GRAP Financial Reporting Framework effectively in order to fully meet the disclosure requirements of these standards.
83. Records management and maintenance disciplines should be refined and included in the daily key controls and reviewed and monitored by the appropriate level of management.

Governance

84. Involvement and oversight of management during the reporting phase should be improved to ensure complete, accurate and timely reporting. In this regard numerous adjustments were made to the financial statements.
85. The municipality did not ensure the establishment of an effective internal audit unit to enhance the internal control environment. The internal audit unit is imperative to ensure the proper implementation and monitoring of internal control.

86. The municipality did not ensure that the audit committee is established. The audit committee is imperative to ensure the proper implementation and monitoring of internal control.

Auditor General

Kimberley

30 November 2014



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence